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Supreme Court, U. S.

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**In the Supreme Court of the United States**

OCTOBER TERM, 1977

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JEANNE HARR AND L. J. HARR, ETC., PETITIONERS

v.

PRUDENTIAL FEDERAL SAVINGS AND LOAN ASSOCIATION

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L. J. HARR, ET AL., PETITIONERS

v.

FEDERAL HOME LOAN BANK BOARD

---

*ON PETITION FOR WRITS OF CERTIORARI TO  
THE UNITED STATES COURT OF APPEALS FOR  
THE TENTH CIRCUIT*

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**BRIEF FOR THE FEDERAL RESPONDENT  
IN OPPOSITION**

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**OPINIONS BELOW**

The opinion of the court of appeals in *Harr v. Prudential Federal Savings and Loan Association* (Pet. App. A-3 to A-10; "the Prudential case") is reported at 557 F. 2d 751, and the opinion of the court of appeals in *Harr v. Federal Home Loan Bank Board* (Pet. App. A-11 to A-18; "the Board case") is reported at 557 F. 2d 747. The order of the district court in the Prudential case (Pet. App. A-19 to A-20) is not reported.



### JURISDICTION

The judgments of the court of appeals were entered on June 27, 1977. A timely petition for rehearing and suggestion for rehearing *en banc* in both cases was denied on July 22, 1977 (Pet. App. A-1 to A-2). The petition for a writ of certiorari was filed on October 20, 1977. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

### QUESTIONS PRESENTED

1. Whether the court in the Prudential case properly concluded that petitioners were attempting to challenge the Home Loan Bank Board's approval of a mutual savings and loan association's plan to convert to a stock association in a proceeding other than that authorized by law.

2. Whether the court in the Board case applied the proper standard of review in concluding that the Board had not abused its discretion in approving the conversion, including the proxy solicitation presenting the planned conversion to shareholders.

### STATUTES AND REGULATION INVOLVED

The relevant provisions of the National Housing Act, the Securities Exchange Act, and the regulations of the Federal Home Loan Bank Board are set forth at Pet. 3-6.

### STATEMENT

1. The Federal Home Loan Board has exclusive authority to charter, supervise, and regulate federal savings and loan associations. Home Owners' Loan Act of 1933, Section 5, 48 Stat. 128, 132, as amended, 12 U.S.C. 1464(a). The Board is authorized under certain conditions to approve the conversion of federal mutual savings and loan associations into state-chartered stock associations. 12 U.S.C. 1464(i); 12 C.F.R. Part 563b.

On December 5, 1963, the Board imposed an administrative moratorium on conversions of federal mutual savings and loan associations into state stock associations because of difficulties encountered with mutual-to-stock conversions under its then-existing regulation. 12 C.F.R. 546.5 (1973 rev.). While the moratorium remained in effect, the Board announced on July 26, 1972, that it would accept, for study purposes, applications to convert from the mutual to the stock form. The announcement specified that the application could provide for distribution of stock by converting associations only to members of record as of July 13, 1972, or earlier (C.A. Rec. 45).

2. On August 4, 1972, the board of directors of Prudential Federal Savings and Loan Association, Salt Lake City, Utah, a federally chartered savings and loan association, adopted a plan of conversion. The plan was filed with the Board on August 6, 1972, and Prudential's depositors were given written public notice on August 10, 1972. The plan provided for the conversion of Prudential into a Utah-chartered savings and loan association through the free distribution of stock to its depositors who had savings accounts at the institution on July 13, 1972 (C.A. Rec. 8-46).<sup>1</sup> Prudential's application thereafter became the subject of administrative, judicial, and legislative proceedings, which centered on the propriety of the proposed free stock distributions.<sup>2</sup>

<sup>1</sup>A free stock distribution is one in which shares of stock in the new corporation are issued to persons who are members of the mutual association on a specified date (the "eligibility record date") without further charges, rather than simply affording such members a priority in the purchase of the shares. See note 5, *infra*; 12 C.F.R. 563b.3(c).

<sup>2</sup>These proceedings included a 1973 amendment to the National Housing Act that imposed a moratorium on mutual-to-stock conversions. Section 402(j) of the National Housing Act, as added, 87 Stat. 343, 12 U.S.C. (Supp. III) 1725(j).

These difficulties were not resolved until Section 402(j) of the National Housing Act was amended in 1974 to permit a limited number of mutual-to-stock conversions prior to June 30, 1976 (Act of October 28, 1974, 88 Stat. 1504, 12 U.S.C. (Supp. V) 1725(j)).<sup>3</sup> Although the Board's conversion regulations then prohibited free stock distributions, the amendment accorded special "grandfather" rights to three savings and loan associations, including Prudential, allowing a free distribution of conversion stock if certain explicit statutory conditions were met. S. Rep. No. 93-902, 93d Cong., 2d Sess. 5 (1974).<sup>4</sup>

In a provision of particular importance to this litigation, the 1974 amendment stated (12 U.S.C. (Supp. V) 1725(j)(4)):

Any aggrieved person may obtain review of a final action of the Federal Home Loan Bank Board \* \* \* which approves, with or without conditions, or disapproves a plan of conversion pursuant to this subsection only by complying with the provisions of subsection (k) of section 1730a of this title within the time limit and in the manner therein prescribed \* \* \*.

In turn, 12 U.S.C. 1730a(k) vests exclusive jurisdiction to review orders of the Board in the United States Courts of Appeals.

The 1974 Act (88 Stat. 1503) also amended Section 12(i) of the Securities Exchange Act of 1934 to transfer administration and enforcement of the registration

<sup>3</sup>The converting institution need not lose its federal charter. 12 U.S.C. (Supp. V) 1725(j)(3).

<sup>4</sup>The conditions were: (1) the application must have been filed with the agency prior to May 22, 1973; (2) the applicant must have "given written public notice to its accountholders of adoption of a plan of

provisions of the Act to the Board with respect to securities issued by all savings and loan associations insured by the Federal Savings and Loan Insurance Corporation. 15 U.S.C. (Supp. V) 78(i).

During the summer of 1975, Prudential conformed its conversion application to the Board's regulations, utilizing July 13, 1972, as the eligibility record date for free distribution of its stock upon conversion.<sup>5</sup> In accordance with the Board's regulations, 12 C.F.R. 563b.4(b), Prudential published notice of the plan on August 15, 1975, inviting "[w]ritten comments, including objections" to the plan (C.A. Rec. 383-388). No member of Prudential filed any objection to the proposed conversion with either the Board or Prudential.

On December 19, 1975, the Board issued an order, Resolution No. 75-1164 (Pet. App. A-21 to A-24), approving Prudential's conversion application. On January 16, 1976, Prudential mailed to its members notice of a special meeting to vote on the plan of conversion, together with proxy material (C.A. Rec. 988). At the special meeting on March 5, 1976, a majority of the total outstanding votes of the association members was cast in the favor of the

conversion" prior to May 22, 1973; and (3) the free stock must be "distributed to accountholders as of a record date prior to the date of such notice." 12 U.S.C. (Supp. V) 1725(j)(2).

<sup>5</sup>Prudential's revised conversion plan called for the issuance of 2,552,000 free shares of nonassessable common stock with a par value of \$1 per share to depositors of record as of July 13, 1972, with one share to be issued for each \$100 in savings balances as of that date. However, the issuance of free stock to directors and principal officers of Prudential was to be based on their savings account balances as of July 20, 1970, the date Prudential's directors first considered a plan of conversion, if the July 20, 1970, balances were less than their savings balances as of July 13, 1972 (C.A. Rec. 992, 995).



conversion (Pet. App. A-16), and Prudential became a federally chartered stock institution in accordance with Board regulations, 12 C.F.R. 563b.6(d).

3. On January 27, 1976, petitioners Jeanne Harr and L.J. Harr filed a complaint in the United States District Court for the District of Utah, seeking to block the conversion (the Prudential case). As summarized by the court of appeals, "[t]he allegations were that a plan to convert to a stock association was part of a conspiracy by the directors to benefit themselves and the officers; that the plan was unfair and itself deceptive; that the proxy material was deceptive; and that Rule 10b-5 of the Securities and Exchange Commission was violated. The complaint also alleged that regulations of the \* \* \* Board were disregarded" (Pet. App. A-4). Although the complaint alleged violations of the securities laws, counsel for the plaintiffs explained at oral argument before the district court that his clients primarily objected to the fairness of the eligibility record date for free stock distribution, since they had either opened new accounts or increased the amount in existing accounts after the record date (February 11, 1976, Hearing Tr. 21-22). The plaintiffs requested judicial amendment of the plan in order to enlarge their share ownership.

The district court granted Prudential's motion to dismiss (Pet. App. A-19 to A-20), and the court of appeals affirmed, holding that the action was in substance a challenge to the fairness and equity of the plan of conversion, review of which was exclusively vested in the court of appeals by 12 U.S.C. (Supp. V) 1725(j)(4) (Pet. App. A-6 to A-7).

In the meantime, on February 20, 1976, all petitioners herein, including borrowers from Prudential, persons who made their first deposits at Prudential after the July 13,

1972, eligibility record date, and depositors who had increased their accounts after that date (Pet. App. A-12), had sought review of Board Resolution No. 75-1164, which approved Prudential's plan of conversion, in the court of appeals (the Board case). Petitioners argued that use of the July 13, 1972, eligibility record date was inequitable to persons who opened or increased the amount in their accounts after that date, that a free distribution of stock was improper, and that the proxy materials were misleading (Pet. App. A-13). The court of appeals rejected these arguments, holding that the Board did not abuse its discretion in approving Prudential's plan, that the July 13, 1972, record date "was mandated by Congress for this conversion" (Pet. App. A-15), and that the free distribution of Prudential's stock had been specifically authorized by statute (Pet. App. A-15). The court of appeals found no omission or misleading statement in the proxy materials sufficient to warrant judicial modification of the plan (Pet. App. A-17).

#### ARGUMENT

1. Petitioners claim that the decisions below merit review because they have "effectively insulated from review by any state or federal court" (Pet. 12) challenges by accountholders to allegedly false and misleading statements made in connection with a proposal that a conversion plan be adopted (Pet. 12-13). That claim is based on a misreading of the Prudential decision. The court of appeals in that case determined that the gravamen of the complaint was a challenge to the conversion plan (Pet. App. A-6 to A-8). Accordingly, it properly affirmed the district court's conclusion that such challenges may be asserted only by a petition in the court of appeals for review of the Board's approval of the plan, pursuant to 12 U.S.C. (Supp. V) 1725(j)(4). Petitioners'

sole stated objection to the proposed conversion in this Court is that the materials distributed by Prudential's management in seeking membership approval of the conversion plan were materially false and misleading. But their abandonment in this Court of objections to the Board's approval of the conversion plan (see, e.g., Pet. 17) does not affect the correctness of the court of appeals' determination that those objections were fundamental to their original complaint; moreover, nothing in the court's opinion suggests that it would have refused to consider challenges to the proxy materials had petitioners presented them independently of their objections to the conversion plan.

Indeed, far from ruling out a private right of action for false and misleading proxy materials issued in connection with a Board-approved plan of conversion, the court of appeals observed, "It must be assumed that the private remedies available under SEC 14A as to fraud also exist under the counterpart [Board] Regulations" (Pet. App. A-5).<sup>6</sup>

The factual conclusion of the court of appeals in the Prudential case that petitioners' suit sought review of the Board-approved plan was correct, and, in any event, does not merit review by this Court. The further conclusion

<sup>6</sup>Since the Prudential decision turned on the specific facts of the case, petitioners err in asserting (Pet. 14-17) that it conflicts with *J.I. Case Co. v. Borak*, 377 U.S. 426, and subsequent cases permitting private suits to vindicate the right of investors to full disclosure of relevant information.

Similarly, the decision does not "eliminate the entire scheme of protection for investors" (Pet. 23) merely by indicating that the 1974 Act transfers to the Board the responsibility for enforcing certain registration provisions of the Securities Exchange Act. See pp. 4-5. *supra*.

that such suits may be brought only by a petition for review in the court of appeals is consistent with the only other federal court rulings on this issue,<sup>7</sup> and is in harmony with rulings of this Court on the exclusivity of similar statutory schemes of review. See *Whitney National Bank in Jefferson Parish v. Bank of New Orleans & Trust Co.*, 379 U.S. 411, 420, and cases cited therein.

2. Petitioners' objection to the decision in the Board case evidently results from their misreading of the holding of the Prudential case, for they assert that the two cases, read together, deny them any opportunity to obtain meaningful judicial review of their claims of fraud in the issuance of the proxy materials (Pet. 15-17, 21).<sup>8</sup> But, as we have shown, the Prudential case does not suggest that such a review would be denied in an appropriate case. Accordingly, there was no need for the court of appeals in the Board case to apply a more stringent standard of review in considering petitioners' claims that the proxy materials were misleading. Instead, the court properly considered only whether the Board had abused its discretion in approving the conversion plan. Since the Board's approval of the proxy materials formed a part of its approval of the plan, petitioners' claims relating to those materials were considered in that context under the

<sup>7</sup>See *Fort Worth National Corp. v. Federal Savings and Loan Insurance Corp.*, 469 F. 2d 47 (C.A. 5), and *Fidelity Financial Corp. v. Federal Savings and Loan Insurance Corp.*, 359 F. Supp. 324 (N.D. Calif.). The Prudential decision does not conflict with *Federal Home Loan Bank Board v. Elliott*, 386 F. 2d 42 (C.A. 9), certiorari denied, 390 U.S. 1011. That case involved an attack on the Board's approval of a plan of merger between two associations, not a mutual-to-stock conversion; no exclusive statutory review procedure similar to that contained in 12 U.S.C. (Supp V.) 1725(j)(4) was applicable.

<sup>8</sup>Indeed, they apparently seek reversal only of the Prudential decision (see Pet. 7-8, 17).

same standard of review.<sup>9</sup> The court found that the Board's approval of the proxy material "was well within the supervisory authority of the Board" (Pet. App. A-16).<sup>10</sup>

Petitioners' suggestion (Pet. 25-27) that the decisions below have a potentially broad impact on the banking community because they cast doubt on the availability of private suits to enforce effective disclosure requirements is incorrect. Indeed, the decisions below do not preclude even private suits alleging material misstatements in proxy materials issued in connection with conversion plans (see pp. 7-9, *supra*,) let alone other private rights of action relating to banking matters.

#### CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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<sup>9</sup>Petitioners apparently agree that the abuse-of-discretion standard is appropriate for review of the Board's decision to approve the conversion (Pet. 17).

<sup>10</sup>As petitioners note (Pet. 15), the court did find the proxy materials misleading in one respect: they indicated that there was an unconditional right to judicial review of the plan. But the court remedied that defect by permitting such review despite the failure to exhaust administrative remedies (Pet. App. A-14).